

REPORT OF EXAMINATION
OF THE
HOMESURE PROTECTION OF CALIFORNIA, INC.
AS OF
DECEMBER 31, 2004

Filed September 13, 2005

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San Francisco, California
May 26, 2005

Honorable John Garamendi
Insurance Commissioner
California Department of Insurance
Sacramento, California

Dear Commissioner:

Pursuant to your instructions, an examination was made of the

HOMESURE PROTECTION OF CALIFORNIA, INC.

(hereinafter also referred to as the Company) at its home office located at 1625 N.W. 136th Avenue, Suite 200, Ft. Lauderdale, Florida 33323.

SCOPE OF EXAMINATION

The previous examination of the Company was made as of December 31, 1999. This examination covers the five-year period from January 1, 2000 through December 31, 2004. The examination included a review of the Company's practices and procedures, an examination of management records, tests and analyses of detailed transactions, and an evaluation of assets and a determination of liabilities as of December 31, 2004, as deemed necessary under the circumstances.

In addition to those items specifically commented upon in this report, other phases of the Company's operations were reviewed including the following areas that require no further comment: fidelity bonds and other insurance; officers', employees' and agents' welfare and pension plans; growth of the company; business in force by states; and sales and advertising.

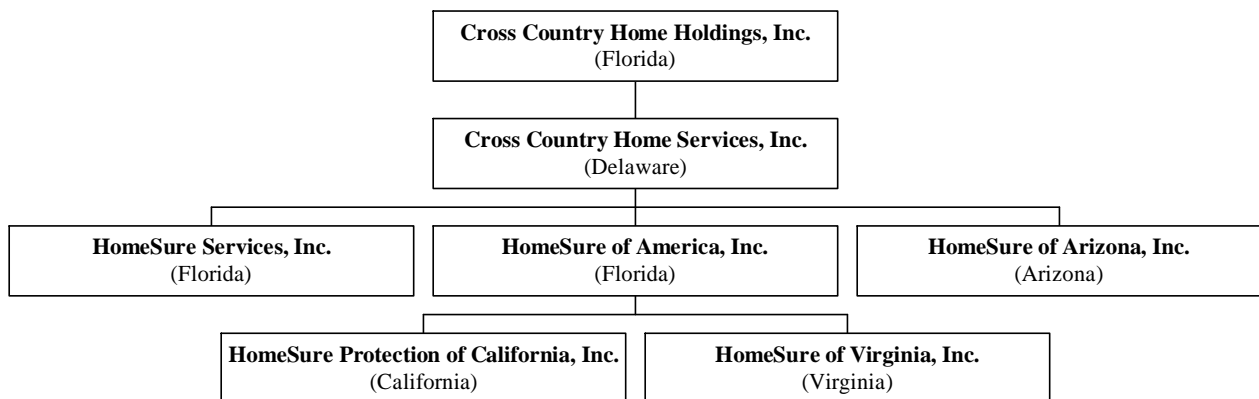
COMPANY HISTORY

HomeSure Protection of California, Inc., then known as Vanguard Warranty Corp. of California, Inc. was incorporated on February 6, 1979 under the laws of the State of California. The Company's name underwent a series of changes as follows: on December 17, 1979 to Security HomeSure Protection Warranty of California, Inc.; on March 27, 1981 to Beacon HomeSure Protection of California, Inc.; on June 22, 1986 to HAA HomeSure Protection of California, Inc.; and on February 26, 1998 to its present name.

Per the terms of an acquisition and merger agreement, approved on February 7, 1997 by the California Department of Insurance, Cross Country Associates, LLC acquired the Homeowners Group, Inc., the indirect parent corporation of the Company. The merger was effective as of June 19, 1997.

MANAGEMENT AND CONTROL

The Company is a wholly-owned subsidiary of HomeSure of America, Inc. The ultimate controlling entity is Cross Country Home Holdings, Inc. ((CCHH)). The following chart depicts the relationship of the Company and its affiliates:



The Company is managed by a four-member board of directors. The following is a listing of the board of directors and principal officers serving at December 31, 2004:

Board of Directors

<u>Name and Residence</u>	<u>Principal Business Affiliation</u>
Howard L. Wolk Brookline, Massachusetts	Vice President Cross Country Home Holdings, Inc.
Jeffrey C. Wolk Brookline, Massachusetts	Vice President Cross Country Home Holdings, Inc.
Nathan T. Wolk Chestnut Hill, Massachusetts	Vice President and Assistant Secretary Cross Country Home Holdings, Inc.
Sidney D. Wolk Boston, Massachusetts	Vice President Cross Country Home Holdings, Inc.

Principal Officers

<u>Name</u>	<u>Title</u>
Sandra C. Finn	President
L. Ashley Coke	Vice President
Thomas C. Canterbury	Vice President
Alfred C. Venditti, Jr	Vice President
Howard L. Wolk	Vice President
Robert W. Judges	Secretary and Treasurer

Management Agreement

The Company does not have any employees. Effective October 1, 1998, the Company modified its existing management agreement with its affiliate, Cross Country Home Services, Inc. (CCHS). Under this agreement, CCHS manages the Company's home warranty business, which includes collection of contract fees, settlement of claims, payment of expenses, accounting and regulatory matters. Under the terms of the agreement, funds held by CCHS shall be held in a fiduciary capacity and paid to the Company within 90 days after collection. Direct costs are reimbursed on an actual cost basis and indirect costs are allocated among the affiliates.

Consolidated Federal Income Tax Agreement

The Company has filed its federal income tax return on a consolidated basis with CCHH per the terms of an informal written agreement until a bona fide agreement was filed on April 8, 2005, with an effective date of March 1, 2005.

CORPORATE RECORDS

California Insurance Code (CIC) Section 735 states, "There shall be entered in the minutes of each such meeting the fact that such officer did so inform the members present." Although the Company informed the board of directors of the 1999 Report of Examination in a Company memo that was signed by the board of directors, the notification was not entered in the minutes. As such, the Company is in violation of CIC Section 735. This violation was also mentioned in the two prior examination reports. It is again recommended that the Company comply with CIC Section 735.

TERRITORY AND PLAN OF OPERATION

The operation of the Company is currently limited to issuing home protection contracts in the State of California. The Company has a management agreement with Cross Country Home Services, Inc. that provides marketing services through HMS National, Inc., an affiliated company. Contracts are also written by third party clients including GMAC Mortgage, Countrywide Mortgage and CitiMortgage. The Company uses Company approved independent contractors throughout California for servicing claims, subject to the oversight and monitoring by the Company's staff. The Company has modified its product and retracted from the marketplace since the previous exam to produce a more profitable product.

Net contract fees written during 2004 totaled \$2,677,328.

REINSURANCE

The Company did not assume or cede reinsurance during the period covered by this examination.

ACCOUNTS AND RECORDS

The Company has not implemented SSAP No. 10 in the reporting and recording of income taxes. The Company reports deferred income taxes for GAAP reporting only. The Company currently records an income tax provision and income tax payable based on the statutory net income of the current year's Annual Statement which is not based on the current year's income tax return. This reporting is not in compliance with SSAP No. 10. Therefore, it is recommend the Company record and report income taxes per SSAP No. 10. The overall effect was not material, as a result, no examination adjustment was made.

FINANCIAL STATEMENTS

The financial statements prepared for this examination report include:

Statement of Financial Condition as of December 31, 2004

Underwriting and Investment Exhibit for the Year Ended December 31, 2004

Reconciliation of Surplus as Regards Contractholders
from December 31, 1999 through December 31, 2004

Statement of Financial Condition
as of December 31, 2004

<u>Assets</u>	<u>Ledger and Nonledger Assets</u>	<u>Assets Not Admitted</u>	<u>Net Admitted Assets</u>	<u>Notes</u>
Bonds	\$4,489,376	\$	\$ 4,489,376	(1)
Cash and short-term investments	502,982		502,982	(2)
Home protection contract fees receivable	1,080,376	554,788	525,588	
Interest, dividends and real estate income due and accrued	<u>42,018</u>	<u></u>	<u>42,018</u>	
Total assets	<u>\$6,114,752</u>	<u>\$ 554,788</u>	<u>\$ 5,559,964</u>	
<u>Liabilities, Surplus and Other Funds</u>				
Claims adjusted and unpaid or in process of adjustment			\$ 119,893	(3)
Other expenses			6,163	
Taxes, licenses and fees			16,700	
Federal income taxes payable			425,598	
Unearned home protection contract fees			1,063,471	
Payable to affiliated companies			58,977	
Advance premiums			<u>3,027</u>	
Total liabilities			1,693,827	
Common capital stock		\$ 20,000		
Gross paid-in and contributed surplus		902,604		
Unassigned funds (surplus)		2,956,032		
Less: Treasury stock, at cost		<u>(12,500)</u>		
Surplus as regards contractholders			<u>3,866,136</u>	
Total liabilities, surplus and other funds			<u>\$ 5,559,964</u>	

Underwriting and Investment Exhibit
for the Year Ended December 31, 2004

Statement of Income

Underwriting Income

Home protection contract fees earned		\$2,423,762
Deductions:		
Claims incurred	\$ 612,902	
Claims service expenses incurred	446,661	
Other expenses incurred	<u>1,111,364</u>	
Total underwriting deductions		<u>2,170,928</u>
Net underwriting gain		252,834

Investment Income

Net investment income earned	\$ 186,078	
Net realized capital gain	<u>9,934</u>	
Total investment gain		<u>196,012</u>
Net income before federal income taxes		448,846
Federal income taxes incurred		<u>(152,608)</u>
Net income		<u>\$ 296,238</u>

Capital and Surplus Account

Surplus as regards contractholders, December 31, 2003		\$4,124,686
Net income	\$ 296,238	
Change in nonadmitted assets	<u>(554,788)</u>	
Change in surplus as regards contractholders for the year		<u>(258,550)</u>
Surplus as regards contractholders, December 31, 2004		<u>\$3,866,136</u>

Reconciliation of Surplus as Regards Contractholders
from December 31, 1999 through December 31, 2004

Surplus as regards contractholders, December 31, 1999, per Examination	\$1,284,662
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	Gain in Surplus	Loss in Surplus
Net income	\$1,119,663	\$
Change in nonadmitted assets	1,473,231	
Prior year adjustment to unrealized losses		11,390
Total gains and losses	\$2,592,864	\$ (11,390)

Increase in surplus as regards contractholders	<u>2,581,474</u>
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Surplus as regards contractholders, December 31, 2004, per Examination	<u>\$3,866,136</u>
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COMMENTS ON FINANCIAL STATEMENT ITEMS

(1) Bonds

The Company's custodian, the Northern Trust Bank of Arizona (NTBA) is not a qualified custodian. Furthermore, the custodian agreement has not been and could not be approved per California Insurance Code (CIC) Section 1104.9 because it does not meet California Department of Insurance (CDI) standards for approval. This violation was also mentioned in the three prior examination reports. Therefore, it was recommended that the company replace the NTBA with a qualified custodian, terminate the NTBA agreement and submit the new agreement to the CDI for approval. The Company stated that effective June 30, 2005 it had transferred the custodial account to Union Bank of California and that it would submit the custodial agreement to the CDI.

(2) Cash and Short-Term Investments

Pursuant to CIC Section 1104.1, Company funds should be deposited in an account located in the State of California. This was also mentioned in the prior examination report. It was recommended that the Company establish either a separate bank account or a fiduciary trust account in the State of California. The Company stated that it was in the process of transferring all of its funds to Union Bank of California.

(3) Claims Adjusted and Unpaid or in Process of Adjustment

A review of the subsequent development of the claim loss reserves found the reserves to be adequate.

SUMMARY OF COMMENTS AND RECOMMENDATIONS

Current Report of Examination

Corporate Records (Page 4): It is recommended that the Company provide the Report of Examination to the board of directors for review in accordance with California Insurance Code (CIC) Section 735.

Accounts and Records (Page 5): It is recommended that the Company record and report income taxes per SSAP 10.

Previous Report of Examination

Management and Control - Consolidated Federal Income Tax Agreement (Page 4): The Company should execute a written federal income tax agreement and file it with the California Department of Insurance (CDI). A written agreement, which became effective on March 1, 2005, was submitted to the CDI on April 8, 2005.

Management and Control - Conflict of Interest (Page 4): The Company should establish a disclosure procedure. The Company has complied with this recommendation.

Corporate Records (Page 4): It was noted in the prior three examination reports that the Company did not comply with CIC Sections 735, 1200 and 1201. The Company has complied with CIC Sections 1200 and 1201 but has not complied with CIC Section 735.

Accounts and Records (Page 6): It was recommended that the Company maintain accurate detailed reports in support of the Company's financial statements. The Company has complied with this recommendation.

Comments on Financial Statement Items – Bonds (Page 11): It was noted in the previous three reports of examinations, that the Company did not have an approved custodial agreement, which

is in violation of CIC Section 1104.9. The Company is in the process of complying with this recommendation.

Comments on Financial Statement Items – Cash and Short-Term Investments (Page 11): Company funds should be deposited in an account located in the State of California pursuant to CIC Section 1104.1. The Company stated that it was in the process of transferring all of its funds to Union Bank of California.

Comments on Financial Statement Items - Receivable from Parent, Subsidiaries and Affiliates (Page 11): It was recommended that the Company stop advancing funds to its parent and affiliates without prior approval pursuant to CIC Section 1215.4 and 1215.5. The Company is in compliance with this recommendation.

ACKNOWLEDGMENT

Acknowledgment is made of the cooperation and assistance extended by the officers and employees of Cross Country Home Services, Inc. during the course of this examination.

Respectfully submitted,

_____/s/____

Sandra Bailey, CFE
Examiner-In-Charge
Senior Insurance Examiner
Department of Insurance
State of California